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| <b>IN RE:</b>                                  | ) |                                  |
|  | ) |                                  |
| <b>JEFFERSON COUNTY, ALABAMA,</b>              | ) | <b>Case No.: 11-05736- TBB-9</b> |
| <b>a political subdivision of the State of</b> | ) |                                  |
| <b>Alabama,</b>                                | ) | <b>Chapter 9 Proceeding</b>      |
|  | ) |                                  |
| <b>DEBTOR.</b>                                 | ) |                                  |
|  | ) |                                  |

Assured Guaranty Municipal Corp., formerly known as Financial Security Assurance Inc. (“Assured”), respectfully submits this Supplemental Statement of Legal Issues (the “Supplemental Statement”) in Support of (I) the Emergency Motion of the Jefferson County Sewer System Receiver For (A) A Determination That the Receiver Shall Continue to Operate and Administer the Sewer System Pursuant to the Receiver Order or (B) For Relief from Automatic Stay or Other Appropriate Relief (the “Receiver’s Motion”), dated November 10, 2011 [Docket No. 40] and (II) the Expedited Motion of Indenture Trustee for Jefferson County’s Sewer Warrants (the “Trustee”) for (A) The Court to Abstain From Taking Any Action to

Interfere with the Receivership Case and the Receiver's Operation and Administration of Sewer System in Accordance with the Receivership Order, or (B) For Relief From the Automatic Stay to the Extent Necessary to Allow Receiver to Continue to Operate and Administer the Sewer System under the Receivership Order, and (C) Request for Expedited Hearing (the "Trustee's Motion," and together with the Receiver's Motion, the "Motions") dated November 10, 2011 [Docket No. 55] and states as follows.<sup>1</sup>

### **I. Background**

1. On November 15, 2011, Assured filed its Statement of Legal Issues in Support of the Motions (the "Statement") [Docket No. 146].

2. On November 16, 2011, Jefferson County, Alabama (the "County") filed its Opposition to the Motions (the "County's Opposition") [Docket No. 189].

3. In its Order, dated November 28, 2011, this Court permitted Assured to file a supplemental brief "on relevant issues that i[t] has not previously addressed in its Memorandum filed on November 15, 2011." [Docket No. 303]. Given the importance of the issue to this case and the municipal finance market in Alabama and nationally, Assured files this Supplemental

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<sup>1</sup> Assured incorporates by reference herein the arguments set forth in the (i) Joinder and Response by Financial Guaranty Insurance Company in Support of the Emergency Motions Filed by the Jefferson County Sewer System Receiver and the Indenture Trustee dated November 15, 2011 [Docket No. 143]; (ii) Response and Memorandum of Supplemental Points of Syncora Guarantee Inc. in Support of: (I) Emergency Motion of the Jefferson County Sewer System Receiver For (A) A Determination that the Receiver Shall Continue to Operate and Administer the Sewer System Pursuant to the Receiver Order or (B) For Relief from Automatic Stay or Other Appropriate Relief, and (ii) Expedited Motion of Indenture Trustee for Jefferson County's Sewer Warrants for (A) The Court to Abstain from Taking Any Action to Interfere with the Receivership Case and the Receiver's Operation and Administration of Sewer System in Accordance with the Receivership Order, or (B) For Relief from the Automatic Stay to the Extent Necessary to Allow Receiver to Continue to Operate and Administer the Sewer System Under the Receivership Order, and (C) Request for Expedited Hearing dated November 15, 2011 [Docket No. 147]; and (iii) Joinder of Certain Liquidity Banks in Support of (1) the Motion of the Jefferson County Sewer System Receiver For (A) A Determination that the Receiver Shall Continue to Operate and Administer the Sewer System Pursuant to the Receiver Order or (B) For Relief from Automatic Stay or Other Appropriate Relief, and (2) Expedited Motion of Indenture Trustee for Jefferson County's Sewer Warrants for (A) The Court to Abstain from Taking Any Action to Interfere with the Receivership Case and the Receiver's Operation and Administration of Sewer System in Accordance with the Receivership Order, or (B) For Relief from the Automatic Stay to the Extent Necessary to Allow Receiver to Continue to Operate and Administer the Sewer System Under the Receivership Order, and (C) Request for Expedited Hearing dated November 18, 2011 [Docket No. 239] (collectively, the "Joinders").

Statement with respect to the appropriate interpretation of section 922(d) of Chapter 9 of Title 11 of the United States Code, 11 U.S.C. §§ 101-1532 (the “Bankruptcy Code”)<sup>2</sup> and its relevance to the application of section 928 of the Bankruptcy Code.<sup>3</sup>

## II. Introduction

4. Section 922(d) of the Bankruptcy Code provides that:

Notwithstanding section 362 of this title and subsection (a) of this section, a petition filed under this chapter does not operate as a stay of application of pledged special revenues in a manner consistent with section [928]<sup>4</sup> of this title to payment of indebtedness secured by such revenues.

11 U.S.C. § 922(d). (emphasis added).

5. The County argues to this Court that section 922(d) only excludes from the automatic stay set forth in sections 362 and 922 of the Bankruptcy Code those revenues that are in the Trustee’s possession as of the date of the County’s bankruptcy petition. [County’s

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<sup>2</sup> Terms not otherwise defined herein shall have the meaning ascribed to them in the Statement.

<sup>3</sup> As described in the Statement, in connection with each claim that Assured has paid or will in the future pay under the Primary Policies or the DSRF Policy, Assured has received and will receive an assignment of all rights of the holders of the insured warrants to the extent of the claim payment and an appointment as agent and attorney-in-fact for the Trustee and each such holder of the insured warrants issued under that certain Trust Indenture between the County and AmSouth Bank of Alabama, dated as of February 1, 1997 (as supplemented and amended, the “Indenture”). Copies of the executed assignments and appointments are attached hereto as Exhibit A. Accordingly, to the extent of claims payments that Assured has made and will continue to make under the Primary Policies or the DSRF Policy, Assured is the real creditor and party-in-interest in this case. In addition, the County has entered into an Insurance Agreement, dated April 1, 2005 with respect to the DSRF Policy (the “Insurance Agreement”). Such Insurance Agreement provides, *inter alia*, that the County (i) agrees to reimburse Assured for all claims paid under the DSRF Policy (plus interest and Policy Costs (as defined therein)) and (ii) “granted and perfected in favor of [Assured] a security interest (subordinate only to that of the owners of the Parity Securities) in all revenues and collateral pledged as security for the Parity Securities.” A copy of the Insurance Agreement is attached as Exhibit D to the Statement. The County has failed to reimburse Assured for any claims paid under the DSRF Policy to date, thus Assured is a direct secured creditor and party-in-interest in this case.

<sup>4</sup> Although section 922(d) actually refers to section 927, “the reference to section 927 is in error” and the proper reference is to section 928 of the Bankruptcy Code. See 6 COLLIER ON BANKRUPTCY ¶ 922.05[3] (16th ed. rev. 2011).

Opposition at 52-53].<sup>5</sup> In the County’s view, the term “pledged” in section 922(d) refers only to such funds and does not reach any revenues not specifically in the possession of the Trustee on the petition date. *Id.* Assured respectfully argues that this interpretation of section 922(d) flies in the face of the plain meaning of the statute, the interpretation of section 922(d) in the context of other relevant provisions of the Bankruptcy Code, the clear legislative history of the Bankruptcy Code and the justified and long-held expectations of the municipal finance markets. The County’s position should be rejected by this Court.

**III. The Plain Meaning of the Term “Pledged” in Section 922(d) is Broad and Encompasses More Than Mere Possession**

6. Section 922(d) specifically references revenues that have been “pledged.” The Bankruptcy Code does not contain a definition of the word “pledge” so the Court must look to relevant non-bankruptcy state law. It is well-settled that courts should look to state law to determine the nature and extent of a security interest. *See Butner v. United States*, 440 U.S. 48, 54-55 (1979) (holding that the existence, nature and extent of a security interest in property is governed by state law); *In re Southern Cal. Plastics, Inc.*, 165 F.3d 1243, 1248 (9th Cir. 1999) (“it is axiomatic that, even in the bankruptcy context, state law governs the validity and extent of liens”); *In re Triple H Auto & Truck Sales, Inc.*, No. 07-13734-MAM-7, 2008 WL 2323921, at \*2 (Bankr. S.D. Ala. June 2, 2008) (“courts must apply state law when determining the extent, validity, and priority of liens and security interests that were created pursuant to state law”) (citing *In re Haas*, 31 F.3d 1081 (11th Cir. 1994)); *In re 1/2 Mile Lumber Co.*, 326 B.R. 876, 881 (Bankr. S.D. Fla. 2005) (“Federal courts are **duty bound** to apply state law when determining the extent, validity, and priority of liens and security interests created pursuant to state law”) (citing

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<sup>5</sup> It appears that the County does not contest that the revenues at issue here are “special revenues” as defined in section 902(2)(A) of the Bankruptcy Code. [County’s Opposition at 52, n. 28].

*In re Haas*, 31 F.3d 1081) (emphasis added).<sup>6</sup> Thus, the plain meaning of the term “pledged” in section 922(d) must be interpreted in accordance with the usage of such term in the relevant state law – in this case the Alabama Code.

7. In the Alabama Code provisions governing municipal finance, it is abundantly clear that the term “pledged funds” is used in a broad fashion and includes all funds or revenues offered as collateral security for the payment of principal and interest on warrants. The Alabama Code typically refers to “pledged funds” or “pledge of pledged funds” to address the creation, perfection and priority of security interests by Alabama counties. The relevant statutes provide:

The pledge of any pledged funds for the payment of the principal of and interest on warrants issued by any county pursuant to this chapter, together with any covenants of such county relating to such pledge, shall have the force of contract between such county and the holders of such warrants. To the extent necessary and sufficient for making the payments secured by any pledge of pledged funds made pursuant to the provisions of this chapter, such pledged funds shall constitute a trust fund or funds which shall be impressed with a lien in favor of the holders of the warrants to the payment of which such pledged funds are pledged. . . . All warrants for which any pledge authorized by the provisions of this chapter may be made shall constitute preferred claims against that portion of the pledged funds so pledged and shall have a preference over any claims for any other purpose whatsoever.

ALA. CODE § 11-28-3. (emphasis added)

Pledged funds. When used with reference to any warrants issued by any county pursuant to the provisions of this chapter, mean any taxes, revenues or other funds pledged pursuant to Section 11-28-3 for the payment of the principal of and interest on such warrants, irrespective of whether such warrants constitute general obligations of such county or limited obligations payable solely from the taxes, revenues or other funds so pledged.

ALA. CODE § 11-28-1.1. (emphasis added)

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<sup>6</sup> The County does not dispute that this Court should look to state law to define the meaning of “pledge.” [See County’s Opposition, at 53 (citing portions of the Alabama Code and Alabama case law)].

8. Thus, pursuant to the Alabama Code, the County was empowered to, and did, pledge and assign “Pledged Revenues” to secure the payment of the warrants. *See* the Official Statement Regarding the Jefferson County, Alabama Sewer Revenue Refunding Warrants, Series 2003-B (the “2003B OS”), at 31; *see also* the Official Statement Regarding the Jefferson County, Alabama Sewer Revenue Refunding Warrants, Series 2003-C (the “2003C OS”), at 29. In particular, the defined term “Pledged Revenues” means “the System Revenues . . . that remain after the payment of Operating Expenses” [2003B OS, at 6; 2003C OS, at 5] and “System Revenues” means “all revenues, receipts, income and other monies . . . received by or on behalf of the County from whatever source derived from the operation of the System . . .” [2003B OS at 7; 2003C OS, at 6 (emphasis added)].

9. Nowhere in the Alabama Code or in the documents defining the security for the warrants is the “pledge” limited to funds in the possession of the Trustee. Quite to the contrary, the plain reading of the pledge reveals that it is broadly written to encompass all revenues received “by or on behalf of” the County that are “derived from the operation of the System.” *Id.*<sup>7</sup> There are simply no temporal or possessory limitations relating to the Trustee defining the “pledge” in any way, shape or form.

10. The County bases its argument that “pledged special revenues” in section 922(d) refers only to revenues in the Trustee’s possession as of the petition date [County’s Opposition, at 54] on Alabama statutes and case law that have no application here,<sup>8</sup> and on statements in

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<sup>7</sup> It is undisputed that the pledge applies to revenues “after payment of Operating Expenses.”

<sup>8</sup> The County attempts to use *Rice v. Garnett*, 84 So. 557, 558 (Ala. Ct. App. 1919) and ALA. CODE § 7-9A-313 cmt. n.5, for support of its assertion that the term “pledge” requires possession. [County’s Opposition, at 54]. However, both the *Rice* case and the statute cited deal with the use of the term “pledge” in the context of the law of bailment and pawns. The definitions in those contexts have no relation to the definition of the term “pledge” in the Alabama laws governing municipal finance. In fact, the County admits that ALA. CODE § 7-9A *et seq.* has no application in this case. [County’s Opposition, at 51, n. 26]. Rather, the Alabama Code provisions governing municipal finance that utilize a broad usage of the term “pledge” without reference to possessory interests governs here.

bankruptcy related commentary that are clearly wrong in this case – at least when considered with the applicable provisions of the Alabama Code cited above.<sup>9</sup> Similarly, the unrelated case law cited by the County for “the general law of pledge” [County’s Opposition at 53] is simply inapposite here in the face of clear and unambiguous statutory provisions governing municipal finance.<sup>10</sup>

11. The case law on point in this area also supports the conclusion that there are no possessory or temporal limitations on a municipal finance “pledge” under Alabama law. *See Heustess v. Hearin*, 104 So. 273, 274 (Ala. 1925)(upholding “pledge” of future revenue stream by municipality because “[t]he term “pledge” in the statute is, of course, not used in the usual sense of a deposit or bailment . . . [i]t means set apart, appropriated, or charged with the payment

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<sup>9</sup> The statement relied on by the County in 6 COLLIER ON BANKRUPTCY ¶ 922.05[2] states that the term pledge “typically denotes a lien obtained by possession.” Whether or not such statement is true in the “typical” case, it clearly does not apply where, as here, the applicable state statutes make possession irrelevant. *See* ALA. CODE § 11-28-1.1 *et seq.* Additionally, other commentators disagree with Collier’s narrow interpretation of section 922(d):

Collier takes a narrow interpretation of section 922(d) which, if correct, would have a serious impact on revenue bondholders . . . Other commentators believe that a broad interpretation of section 922(d) is warranted by the legislative history of this section . . . First, the Committee on the Judiciary of the Senate directly addressed this point in its report stating:

[T]he automatic stay that becomes effective against creditors of a municipality is made inapplicable to the payment of principal and interest on municipal bonds paid from pledged revenues. In this context, pledged revenues includes funds in the possession of the bond trustee as well as other pledged revenues.

Moreover, the entire rationale for section 922(d) as explained above, is that it would be needlessly disruptive to financial markets to apply the automatic stay to the payment of revenue bonds.

Chapter 9 of the Bankruptcy Code: A Viable Option for Municipalities in Fiscal Crisis?-The Urban Lawyer Volume 24, No. 3, at 572-73 (Summer 1992).

<sup>10</sup> The County cites to *Security Warehousing Co. v. Hand*, 206 U.S. 415, 421 (1907) and *In re Interstate Dep’t Stores, Inc.*, 128 B.R. 703, 705 (Bankr. N.D.N.Y. 1991) for the proposition that the general law of pledge requires possession. [County’s Opposition, at 53-54]. However, both those cases are clearly using the term “pledge” in the context of the common law of bailment which has absolutely no relation to the term “pledge” in the municipal finance context. *See* ALA. CODE § 11-28-1.1 *et seq.*; [see also County’s Opposition, at 51-52 and n. 26].

of a specific obligation authorized by law . . . funds to accrue in future may be, and continually are, pledged by counties . . . to secure bonds, warrants . . .”).

12. Thus, the plain meaning of the term “pledged special revenues” in section 922(d) when interpreted in light of applicable Alabama statutes and relevant case law does not require any possessory interest and should be broadly construed to encompass all revenues received “by or on behalf of the County” that are “derived from the operation of the System,” whether received by the County or the Receiver, either pre or post-petition.

**IV. The Inclusion of Section 928 in the Bankruptcy Code Supports the Conclusion That “Pledged Special Revenues” in Section 922(d) Refers To All Revenues, Not Only Those Revenues in the Trustee’s Possession**

13. The term “pledged special revenues” in section 922(d) must refer to all special revenues,<sup>11</sup> including special revenues obtained post-petition, and not only those revenues held by the Trustee as of the petition date. Any other interpretation of section 922(d) would negate section 928 of the Bankruptcy Code.

14. The County acknowledges that sections 922(d) and 928 of the Bankruptcy Code must be read together [County’s Opposition at 56], however, the County glosses over the fact that its interpretation of section 922(d) completely contradicts the purpose of section 928 of the Bankruptcy Code. Section 928 of the Bankruptcy Code provides that all special revenues acquired by a debtor after the commencement of the case will remain subject to the “lien” entered into by the debtor prior to commencement of the bankruptcy case, notwithstanding section 552(a) of the Bankruptcy Code.<sup>12</sup> The purpose of section 928 is to make it easier for

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<sup>11</sup> References to “all special revenues” herein are to “the System Revenues . . . that remain after payment of Operating Expenses.” [2003B OS, at 6; 2003C OS, at 5].

<sup>12</sup> Section 928 provides:

(a) Notwithstanding section 552 (a) of this title and subject to subsection (b) of this section, special revenues acquired by the debtor after the commencement of the case shall remain subject

municipalities to obtain financing for public projects by preserving, after the filing of a bankruptcy petition, the preexisting relationship between the municipal obligor and warrant holders in which warrant holders have the right to be paid from the municipalities' pledged revenue stream but not from the general funds of the municipality. *See S. Rep. No. 100-506*, 100th Cong., 2d Sess., at 4, 8 (1988) (the "Senate Report").

15. The term "lien" is defined in section 101(37) of the Bankruptcy Code as a "charge against or interest in property to secure payment of a debt or performance of an obligation." 11 U.S.C. § 101(37). The nature and extent of any "lien" under the Bankruptcy Code is determined by applicable state law. *See In re Triple H Auto & Truck Sales, Inc.*, 2008 WL, at \*2 ("courts must apply state law when determining the extent, validity, and priority of liens and security interests that were created pursuant to state law") (citing *In re Haas*, 31 F.3d 1081); *In re 1/2 Mile Lumber Co.*, 326 B.R. at 881 ("Federal courts are duty bound to apply state law when determining the extent, validity, and priority of liens and security interests created pursuant to state law") (citing *In re Haas*, 31 F.3d 1081) (emphasis added). In this case, the applicable state law is Alabama Code § 11-28-3 ("pledged funds shall constitute a trust fund or funds which shall be impressed with a lien in favor of the holder of warrants to the payment of which such pledged funds are pledged . . .") (emphasis added). Thus, under the Alabama Code, the "pledge" by the County created the "lien" in favor of the holders of warrants.

16. If section 922(d) is applied in accordance with the County's interpretation, then section 928 makes little sense since, according to the County, the "pledge" extends only to

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to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

(b) Any such lien on special revenues, other than municipal betterment assessments, derived from a project or system shall be subject to the necessary operating expenses of such project or system, as the case may be.

11 U.S.C. § 928.

Trustee-held funds on the petition date. Under this interpretation, there is no “pledge” to support the state-law created “lien” on post-petition revenues that section 928 purports to maintain for the benefit of warrant holders. This is simply an illogical reading of the Bankruptcy Code. Section 922(d) must be read in conjunction with section 928. If section 928 of the Bankruptcy Code is to have any significance in preserving state-law created liens on post-petition revenues, the only logical interpretation of section 922(d) is that the automatic stay is inapplicable to all pledged special revenues (interpreted by reference to applicable state law), whether held by the Trustee or otherwise, including revenues received by the County or the Receiver post-petition, throughout the chapter 9 case.<sup>13</sup>

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<sup>13</sup> Venturing even further afield from issues relevant to the Motions, the County asserts, without citing any authority, that the provision in section 928(b) stating that the lien on post-petition revenues referenced in section 928(a) “shall be subject to the necessary operating expenses of the project or system” is somehow broader than the definition of “Operating Expenses” in the Indenture. [County’s Opposition at 55]. The County asserts, again without authority, that because the Trustee’s lien on post-petition revenues is subject to this so-called “surcharge,” that net revenues available post-petition for payment to warrant holders under section 928(b) are less than net revenues available for such payment under the Indenture. [County’s Opposition at 56]. This unsupported assertion could not be more wrong.

The legislative history of section 928(b) as well as the Report of the National Bankruptcy Conference on the Municipal Bankruptcy Amendments clearly states that the definition of “operating expenses” in section 928(b) does not displace a net revenue pledge that provides for the payment of operating expenses before the payment of principal or interest.

The legislative history to section 928 provides that:

The intent of Subsection (b) is not to change the priority or intent of the use of special revenues under the terms of the municipal debt financing documents.

Subsection (b) sets forth a minimum standard for paying operating expenses ahead of debt service where revenues are pledged. It is not intended to displace any broader standard contained in the terms of the pledge or applicable nonbankruptcy law.

Senate Report at 23 (emphasis added).

More importantly, both the legislative history and the Report of the National Bankruptcy Conference on the Municipal Bankruptcy Amendments provide that the purpose of section 928(b) is to provide for the payment of operating expenses in situations in which there is a gross revenues pledge with no provision for the payment of operating expenses. The Report of the National Bankruptcy Conference makes the point succinctly:

Subsection (b) . . . provides for the payment from pledged special revenues of operating expenses of the project or system producing the revenues before use of those revenues to pay interest or

V. **The Legislative History Could Not Be Clearer that “Pledged Special Revenues” in Section 922(d) Includes Revenues in the Possession of the County or the Receiver**

17. Contrary to the County’s assertions [*See* County’s Opposition, at 52-53], the legislative history to both the Municipal Bankruptcy Amendments as well as other sections of the Bankruptcy Code make clear that the term “pledged special revenues” in section 922(d) was intended to include revenues that are not in the Trustee’s possession.

A. **Legislative History to the Municipal Bankruptcy Amendments**

18. The legislative history to the Municipal Bankruptcy Amendments states that the term “pledged revenues” was to be broadly defined to include all revenues, regardless of possession. The Senate Report provides that

[T]he automatic stay that becomes effective against creditors of a municipality is made inapplicable to the payment of principal and interest on municipal bonds paid from pledged revenues. **In this context, “pledged revenues” includes funds in the possession of the bond trustee as well as other pledged revenues.**

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principal on the bonds. In very general terms, a net revenue pledge would survive, and a gross revenue pledge would be treated as if it were a net revenue pledge.

Legislation to Amend Chapter 9 of the Bankruptcy Code, *Hearing Before the Subcomm. on Monopolies and Comm. Law of the House Judiciary Comm. On H.R. 3845*, 100<sup>th</sup> Cong. 2d Sess., Ser. No. 73, at 45-48 (Report of the National Bankruptcy Conference on Proposed Municipal Bankruptcy Amendments) (emphasis added).

Collier is in accord with this interpretation of section 928(b):

In order to prevent the recognition and enforcement of a lien on special revenues contained in section 928(a) from becoming oppressive in those states in which a court would enforce a gross revenue pledge, section 928(b) permits recognition and enforcement only to the extent of the equivalent of a net revenue pledge.

6 COLLIER ON BANKRUPTCY ¶ 928.03.

Finally, this interpretation comports with the plain language of section 922(d) which exempts pledged special revenues from the automatic stay when applied “in a manner consistent with section [928].” 11 U.S.C. § 922(d). It is abundantly clear that this phrase in section 922(d) supports application of pledged special revenues only after payment of operating expenses in the case of a gross revenue pledge. Once again, sections 922(d) and 928, when properly construed, are perfectly consistent.

*Senate Report*, at 13 (emphasis added). The Senate Report goes on to inform us that:

Reasonable assurance of timely payment is essential to the orderly marketing of municipal bonds and notes and continued municipal financing.

Where the pledge of revenues survives section [928], it would be needlessly destructive to financial markets for the effectuation of the pledge to be frustrated by the automatic stay . . . .

*Senate Report*, at 21.

Thus, the legislative history to the Municipal Bankruptcy Amendments explicitly provides that “pledged revenues” includes “pledged revenues” other than those in the hands of the Trustee, *i.e.*, in this case the revenues in the hands of the County or the Receiver, and that such revenues should be applied to the payment of debt service on the warrants during the pendency of the chapter 9 case.

## **B. Legislative History to Bankruptcy Code Section 552**

19. In addition to the legislative history of the Municipal Bankruptcy Amendments, the legislative history to other sections of the Bankruptcy Code further supports the conclusion that “pledged special revenues” in section 922(d) cannot refer only to funds held by the Trustee at the petition date. For example, the legislative history to section 552 of the Bankruptcy Code describing the treatment of hotel revenues provides:

Section 214 also clarifies the bankruptcy treatment of hotel revenues which have been used to secure loans to hotels and other lodging accommodations. These revenue streams, while critical to a hotel’s continued operations, are also the most liquid and most valuable collateral the hotel can provide to its financiers . . . . [A]mong other things, the reference to section 363 permits use of **pledged revenues** if adequate protection is provided; the reference to section 506(c) permits broad categories of operating expenses--such as the cost of cleaning and repair services, utilities, employee payroll and the like--to be charged against pledged revenues . . . .

140 Cong. Rec. 142 (Tuesday, October 4, 1994) (emphasis added).

20. Congress's reference to "pledged revenues" in the legislative history to section 552 refers to the debtor's use of "pledged revenues" received by and in the possession of the debtor. Consistent with section 552, the term "pledged special revenues" in section 922(d) is clearly intended to include those revenues in the possession of the County or the Receiver and not limited to revenues in the possession of the Trustee on the petition date.

**VI. The Justified and Long-Held Expectations of the Municipal Finance Market Support A Broad Interpretation of Section 922(d)**

21. On November 17, 2011, the Securities Industry and Financial Markets Association submitted a letter to the Court to alert the Court of issues that may potentially have significant negative municipal securities market implications (the "SIFMA Letter"). The SIFMA Letter makes clear that an integral part of municipal financing is the assurance that purchasers of revenue warrants secured by special revenues will continue to receive principal and interest payments if the municipality enters chapter 9. In fact, the SIFMA Letter points out, the Municipal Bankruptcy Amendments were enacted for the purpose of reassuring the market that pledged revenues will continue to be collected for payment to warrant holders during the chapter 9 case. Additionally, the SIFMA Letter notes that a municipality's representation to the market is very important to market stability. Any attempt to change a previous representation to the market that a lien pledged to holders of special revenue warrants will continue through a chapter 9 proceeding and that the payments collected will be applied as prescribed would create market uncertainty and confusion. Such uncertainty and confusion would defeat the primary purpose of the Municipal Bankruptcy Amendments -- to ensure the stability of the municipal securities market. A copy of the SIFMA Letter is attached hereto as Exhibit B. Similar concerns have been widely reported in the national press. *See, e.g.* Kelly Nolan, *Muni Market Sounds Alert*,

*Alabama County's Bankruptcy Filing May Imperil Payments to Some Bondholders*, Wall St. J. (November 29, 2011) (attached hereto as Exhibit C).

22. Market expectations are particularly sensitive and relevant in this case. In each Official Statement issued for the sale of each series of warrants, the County represented that:

A petition filed under Chapter 9 of the Bankruptcy Code, however, does not operate as a stay of application of pledged special revenues to payment of debt secured by such revenues. Thus, an automatic stay under Chapter 9 would not be effective to prevent payment of principal and interest on the [Warrants] from the Pledged Revenues.

[2003B OS, at 32; 2003C OS, at 30 (emphasis added)].

23. The County should not be permitted to abrogate this promise through a tortured interpretation of the Bankruptcy Code and its legislative history – particularly where a direct and logical reading supports the market's expectations.

**VII. Section 904 Does Not Preclude the Court From Enforcing Section 922(d)**

24. For all the reasons discussed above, it is clear that the exception to the automatic stay in section 922(d) includes all of the revenues derived from the sewer system, rather than just those revenues in the possession of the Trustee. However, the County further argues that notwithstanding sections 922(d) and 928 of the Bankruptcy Code, section 904 of the Bankruptcy Code prohibits the Court from requiring the County to make payments to creditors in accordance with the Receivership Order and the governing indenture. The County states in the County's Opposition that section 922(d) "does not, on its face, require the County to remit Net System Revenues collected by the County *after* the Filing Date to anyone, particularly given the broad proscription against interference with 'any of the property or revenues of the debtor' contained in Bankruptcy Code section 904(2)." [County's Opposition at 52-53].

25. A chapter 9 debtor may not determine which chapter 9 provisions it will or will not comply with. *See In re County of Orange*, 191 B.R. 1005 (Bankr. C.D. Cal. 1995); *In re City*

of *Vallejo, California*, Case No.: 08-26813-A-9 Memorandum Opinion (E.D. Cal. March 13, 2009) [Docket No. 473] (The “Memorandum Opinion”). In *Orange County* and the *City of Vallejo*, the courts clearly stated that when a municipality submits itself to the jurisdiction of the bankruptcy court by filing a chapter 9 petition, it is subject to all provisions in chapter 9. “By authorizing the use of chapter 9 by its municipalities, [the debtor] must accept chapter 9 in its totality; it cannot cherry pick what it likes while disregarding the rest.” *County of Orange*, 191 B.R. at 1021; *see also* 6 COLLIER ON BANKRUPTCY ¶ 903.02[4].

26. In *City of Vallejo*, the City filed a motion to reject collective bargaining agreements with certain of its unions pursuant to section 365 of the Bankruptcy Code, which is made applicable in chapter 9 cases by section 901. *See generally Memorandum Opinion*. Various unions and state pension organizations opposed the City’s motion and argued that the application of section 365 in chapter 9 should be restricted by state labor law and restrictions regarding the rejection of collective bargaining agreements in chapter 11. *See Id.* The court found that unexpired collective bargaining agreements are subject to rejection under section 365 as Congress incorporated section 365 into chapter 9 without restricting its application to collective bargaining agreements. *Id.* at 7-8. “Consequently, if a municipality is authorized by the state to file a chapter 9 petition, it is entitled to fully utilize 11 U.S.C. § 365 to accept or reject its executory contracts.” *Id.* at 4.

27. Similar to *City of Vallejo* and *Orange County*, the County cannot use section 904 to preclude the Court from enforcing specific provisions of chapter 9, such as sections 922(d) and 928. The County filed a chapter 9 petition and may not cherry pick which provisions it chooses to follow; the County is subject to all provisions of chapter 9. The Court may thus

enforce sections 922(d) and 928 of the Bankruptcy Code notwithstanding the provisions of section 904.

28. Finally, nothing in the language of section 904 or the case law interpreting it even suggests that it can be used to shield the debtor from otherwise enforceable contractual obligations to creditors where the automatic stay does not apply or has been lifted or modified. This Court should not let the County do so here.

### **VIII. Conclusion**

WHEREFORE, Assured respectfully requests, based on the legal authorities and facts set forth in the Motions, the Statement and the Joinders (and incorporated herein by reference) and in this Supplemental Statement, that the Court enter an order (i) granting the requests for relief set forth in the Motions; and (ii) granting any such other relief as the Court deems just and proper.

This the 2nd day of December, 2011.

Respectfully submitted,  
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